**Assessing the risks of developing social infrastructure through social finance**

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*Abstract*

This presentation will begin with a brief description of social finance, and an explanation about why it is important to pay attention to social finance as a growing source of (primarily private, at times combined with public) funding for social infrastructure in both developed and emerging markets. It will then lay out some of the key risks involved with using social finance as a mechanism for developing social infrastructure, particularly in emerging markets. Analyzing one of the best studied examples of social finance, microfinance, the presentation will focus on the risk of “mission drift,” which materializes when microfinance institutions (MFIs), originally conceived with a strong social mission to develop social infrastructure through the mechanism of “inclusive finance”, gradually come to prioritize a commercial mission, sometimes with grave human consequences.

The presentation will tell the story of one (among several) large MFI in India that, in an effort to attract capital needed to grow its operations, went through an initial public offering process, thereby diversifying its shareholder base and altering its governance. These structural shifts produced changes in the operations of the MFI, in particular in the form of lower due diligence standards. In short, structural changes in the governance of the institution generated incentives to extend more loans to more (or the same) individuals without sufficient regard for their ability to repay. Pressure to ensure repayment, sometimes through coercive collection practices, was also generated as a result of the governance shifts. Over-indebtedness became a problem of explosive proportions in the state of Andhra Pradesh and the government of that state took (highly criticized) aggressive measures to stem it.

The events that ensued and the regulatory responses that followed sent violent ripples of concern across the microfinance industry, and, in many ways, everybody lost: the MFIs operating in India, the microfinance industry globally, those MFI investors who had hoped to be deploying their investments toward achieving social good (while making a commercial return), but most importantly, those individuals who were the intended beneficiaries of inclusive finance, namely, the borrowers of micro-loans.

This case highlights the risk of mission drift, as well as the risks attached to having inadequate regulatory structures and mechanisms in place for preventing and reacting to drifts. Lessons can and should be drawn from this experience to better inform the regulation of social finance more broadly.

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